

**Statement of Michael Brostek,  
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Thank you for inviting me to serve on today's panel and for the opportunity to contribute to the discussion as the Commissioner of Internal Revenue prepares to make recommendations later this year on ensuring high quality service to taxpayers by the paid preparer community. Paid tax return preparers provide service to tens of millions of taxpayers annually and are a critical part of the nation's tax administration system. They offer a wide variety of assistance, including help understanding tax obligations, and return preparation and electronic filing. In 2007, 59 percent of individual taxpayers had their returns prepared and filed by paid preparers. Currently, only a few Internal Revenue Code provisions apply to all paid preparers and only a small portion of paid preparers—enrolled agents—have any federal registration, testing, or fee requirements.

Over the course of several years, GAO has developed a wide body of work on issues pertaining to paid preparers. In 2002, we estimated that as many as 2.2 million tax returns claimed the standard deduction when claiming itemized deductions would have been more beneficial.<sup>1</sup> These taxpayers may have overpaid their taxes by nearly a billion dollars. About half of these tax returns were prepared by a third party. In 2005, we reported that approximately 447,000 suboptimal choices were made among available postsecondary education tax preferences by either not claiming a credit or claiming one that was less advantageous to the taxpayer.<sup>2</sup> We estimated that over half of these returns were prepared by paid preparers.

In 2006, we testified before Congress on the results of an undercover investigation where we identified mistakes in 19 out of 19 visits to paid preparers working in preparer chain offices.<sup>3</sup> Some of the mistakes were significant, either exposing the taxpayers to serious IRS enforcement action or costing taxpayers over \$1,500 in overpaid taxes. In 10 of the 19 cases, preparers did not report cash side income that our taxpayers said they had earned. Even in cases where the side income was reported, several paid preparers gave us incorrect information. Several advised us that reporting such income was our decision because IRS would not know of it unless we reported it. One preparer told our investigator posing as a sales worker that she did not have to report the income unless it was over \$3,200. According to IRS officials we spoke with concerning our visits, although IRS seldom has clear evidence about what transpires between a preparer and a taxpayer, if IRS were to uncover problems with the preparation of real tax returns similar to several that we found, the preparers would be subject to civil sanctions. IRS officials also said that although the dollar amounts of errors made by the practitioners might not result in prosecutions, criminal sanctions such as willful preparation of a false or fraudulent return might apply. Findings from this work led us to recommend that IRS conduct necessary research to determine the extent to which paid preparers live up to their responsibility to file accurate and complete tax returns based on information they obtain from their customers.

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<sup>1</sup> GAO, *Tax Deductions: Further Estimates of Taxpayers Who May Have Overpaid Federal Taxes by Not Itemizing*, GAO-02-509 (Washington, D.C.: Mar. 29, 2002)

<sup>2</sup> GAO, *Student Aid and Postsecondary Tax Preferences: Limited Research Exists on Effectiveness of Tools to Assist Students and Families through Title IV Student Aid and Tax Preferences*, GAO-05-684 (Washington, D.C.: July 29, 2005)

<sup>3</sup> GAO, *Paid Tax Return Preparers: In a Limited Study, Chain Preparers Made Serious Errors*, GAO-06-563T (Washington, D.C.: Apr. 4, 2006)

In March 2008, we reported that IRS faces limitations in identifying individual paid preparers and monitoring their performance.<sup>4</sup> As a result, we recommended IRS develop a plan to require a single identification number for paid preparers. Also last year, we reported on paid preparer regulations in California and Oregon—two states that for many years have had their own requirements that apply to paid preparers working in their states.<sup>5</sup> According to our analysis IRS tax year 2001 NRP data, Oregon returns were more likely to be accurate while California returns were less likely to be accurate compared to the rest of the country after controlling for other factors likely to affect accuracy. These results are consistent with, but do not prove, that Oregon's regulations led to some increased tax return accuracy. It is important to note that our analysis could not account for all factors that might affect the accuracy of these tax returns. Because some states without preparer regulation also had tax returns that, on average, were more accurate than the national average, some portion of the increased accuracy of Oregon returns likely is due to other factors. We also said that if only a small portion of the increased revenue in Oregon is attributable to the Oregon regulatory regime, the regime would compare favorably to IRS's overall efforts to increase reporting accuracy. Consequently, we said that if Congress judges that the Oregon paid preparer regulatory regime is likely to account for at least a modest portion of the higher accuracy of Oregon federal tax returns and could be implemented nationwide at a favorable cost compared to the potential benefits of improved accuracy, it should consider adopting a similar regime nationwide. In addition to California and Oregon, other states have either enacted—or have considered enacting—paid preparer regulations.

While our reports mention many errors on returns filed by paid preparers, we have also said not all of these errors are necessarily the preparer's fault; the taxpayer may be to blame. Ultimately, preparers must depend on the information provided by the taxpayer in order to accurately prepare returns.

In closing, paid preparers are such an important part of the federal tax administration system that IRS sometimes refers to them as "partners." The tax system likely could not function without them. However, poorly performing paid preparer errors have the potential to cause significant harm both to taxpayers and the federal government. As our work has indicated, millions of tax returns prepared by paid preparers have serious compliance problems, which often leave taxpayers owing or overpaying by hundreds or thousands of dollars and/or be subject to IRS enforcement action. When mistakes or deliberate noncompliance by paid preparers result in taxpayers underreporting their tax liabilities, it adds to the tax gap. Unscrupulous and incompetent preparers also compete unfairly with accurate preparers and mistakes or deliberate noncompliance erodes taxpayer confidence in the tax system.

I would like to thank you again for the invitation to participate in today's session. I look forward to the discussion.

#### GAO Reports and Testimonies Related to Paid Preparers

GAO, *Tax Administration: Many Taxpayers Rely on Tax Software and IRS Needs to Assess Associated Risks*, GAO-09-297 (Washington, D.C.: Feb. 25, 2009)

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<sup>4</sup> GAO, *Internal Revenue Service: Fiscal Year 2009 Budget Request and Interim Performance Results of IRS's 2008 Tax Filing Season*, GAO-08-567 (Washington, D.C.: Mar. 13, 2008)

<sup>5</sup> GAO, *Tax Preparers: Oregon's Regulatory Regime May Lead to Improved Federal Tax Return Accuracy and Provides a Possible Model For National Regulation*, GAO-08-781 (Washington, D.C.: Aug. 15, 2008)

*GAO, Tax Preparers: Oregon's Regulatory Regime May Lead to Improved Federal Tax Return Accuracy and Provides a Possible Model For National Regulation, GAO-08-781 (Washington, D.C.: Aug. 15, 2008)*

*GAO, Internal Revenue Service: Fiscal Year 2009 Budget Request and Interim Performance Results of IRS's 2008 Tax Filing Season, GAO-08-567 (Washington, D.C.: Mar. 13, 2008)*

*GAO, Paid Tax Return Preparers: In a Limited Study, Chain Preparers Made Serious Errors, GAO-06-563T (Washington, D.C.: Apr. 4, 2006)*

*GAO, Student Aid and Postsecondary Tax Preferences: Limited Research Exists on Effectiveness of Tools to Assist Students and Families through Title IV Student Aid and Tax Preferences, GAO-05-684 (Washington, D.C.: July 29, 2005)*

*GAO, Tax Administration: Most Taxpayers Believe They Benefit from Paid Tax Preparers, but Oversight for IRS Is a Challenge, GAO-04-70 (Washington, D.C.: Oct. 31, 2003)*

*GAO, Tax Deductions: Further Estimates of Taxpayers Who May Have Overpaid Federal Taxes by Not Itemizing, GAO-02-509 (Washington, D.C.: Mar. 29, 2002)*